SCHOOL BUSINESS ALERT

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M & M PRODUCTIONS
(McCurdy & Meyer Budget/CAR Workshops)

Gary Meyer, Department of Management, and Su McCurdy, Department of Education, will again be presenting a joint workshop. The topics will be the FY96 Aid and Levy Worksheet, FY96 Certified Budget Papers, GAAP Fund basics, sorting out the Activity Fund, and highlights of reporting problems or changes on the CAR.

The workshops are scheduled early in the year in order for Gary and Su to be available to the legislature during the time they might be dealing with the finance formula. The schedule is:

DATE	TIME	PLACE
Tuesday, January 3	12:30-4:30	AEA 3 Cylinder
Wednesday, January 4	8:30-12:30	AEA 5 at Colonial Inn Fort Dodge
Thursday, January 5	8:30-12:30	AEA 12 Martin North Sioux City
Friday, January 6	8:30-12:30	AEA 13 Halvorson Conf. Center Council Bluffs
Monday, January 9	12:30-4:30	AEA 15 Bldg 41, Rm. 209 Ottumwa
Tuesday, January 10	12:30-4:30	AEA 9 Conf. Rm B Bettendorf
Wednesday, January 11	12:30-4:30	AEA 10 Cedar Rapids
Thursday, January 12	8:30-12:30	AEA 1 at Central State Bank Drive-up, North Main St. Elkader
Friday, January 13	8:30-12:30	AEA 7 Conf. Rm. A Cedar Falls
Tuesday, February 14	12:30-4:30	AEA 11 Johnston

For FY96 the statutory fund groupings of General and Schoolhouse no longer exist. The FY96 budget papers and instructions have been redesigned to reflect the new GAAP funds and to be more user friendly. The "CAR to Budget" crosswalk has also been redesigned into an easy-to-read report format.

PERSONNEL FILES

Department staff would like to create a list of items required or recommended to be present in personnel and payroll files. If you feel comfortable with your files, will you please send a listing of items you keep in personnel and/or payroll files with the reason for the item (such as identifying the internal revenue code citation, federal law, state law, state rule, board policy, master contract, etc.). Send to Susan McCurdy, Bureau of School Administration and Accreditation, Department of Education, Grimes State Office Building, Des Moines, Iowa 50319-0146. A copy of the completed list will be made available to all districts.

FOSTER CARE PUPILS AND CLAIMS

In the August issue of *School Business Alert*, nonpublic textbooks and claims were discussed. In this issue, foster care pupils and related claims for reimbursement will be addressed.

The education of and payment for children living in foster care facilities is covered in chapter 282 of the Iowa Code. There are three different types of funding:

1 for a student, whether special education or regular education, who is living in a foster care facility which is located in the **same** school district where the student resided before receiving foster care.
2. for a student who is receiving **special education** services and who is living in a foster care facility which is located in a school district which is **not the same** school district where the special education student resided before receiving foster care.
3. for a student who is **not receiving special education services** and who is living in a foster care facility which is located in a school district which is **not the same** school district where the student resided before receiving foster care.

In the first situation, where the facility is located within the student's own district of residence, the fact that the student is living in a facility is not relevant. Counting and funding does not change.

The second situation, where the facility is located in a district other than the student's own district of residence and the student is receiving special education services, is handled by the bureau of special education and will not be discussed here

The third situation, where the facility is located in a district other than the student's own district of residence and the student is not receiving special education services, will be the situation discussed in this article.

The district in which the facility is located counts all regular education students living in that facility, whether resident or not, if enrolled in the district on the third Friday in September. Also, the number of regular education students living in that facility on count day and enrolled in the district, but who were not residents of the district before entering foster care, is indicated on Item 2, Form M, page 10 of the Certified Enrollment form. This information will be used by the Department of Education to figure the claim amount at the end of the year.

The serving district keeps the same attendance records (aggregate days present and absent) on these students as any other students, noting that these students and all subsequent students enrolling in the district throughout the school year are foster care students who were not residents of the district prior to entering foster care.

On June 30, the district board determines if a claim is necessary. This is done by multiplying the number of students indicated on Item 2, Form M, page 10 of the Certified Enrollment form by 9, and comparing that product to the aggregate months of attendance of all regular education students in foster care who were not residents of the district prior to entering foster care. If the latter figure is larger, the district files a claim with the Department of Education. That claim is located on Part 1 of the Certified Annual Report (CAR). The district receives 1/9 of its district cost per pupil for every month that the aggregate months of attendance on students served exceeds the aggregate months of students counted. The claim is paid by October 1 and comes off the top of state foundation aid to all school districts.

The calculation of the claim has been so complicated, causing much difficulty for districts, that the Department of Education will make the determination and calculation on behalf of district beginning in Fiscal Year 1994-95. Information will come from the Certified Enrollment form and the CAR and will use the aggregate **days** of attendance and absence records that the district already is required to collect on served students. The DE will calculate aggregate months, the difference, and the claim amount by computer and relay the information to the Department of Revenue and Finance electronically.

Independent auditors are required by Iowa Code to audit the CAR and the Certified Enrollment. The foster care facilities claim is part of both forms. The information used to determine the counts of students and aggregate days should be made available to the auditor as part of the audit procedures

AUDITS

Each year the audits show improvement in financial management and office procedures by districts, and this year is no exception. Only a few corrective action plans have been needed, and most responses have been prompt and acceptable.

Common audit comments seem to be grouped into three areas:
1. Reportable conditions in the letter on internal controls require district responses which tell what the district intends to do to correct or reduce the problems. Responses about "cost-benefit" and "lack of money to hire additional staff" are not appropriate. Management is required to maintain a system of internal controls. Telling what the district cannot do is insufficient. The district needs to tell what it will do to strength internal controls: board audit committees, additional administrative reviews, reassign job responsibilities, etc
2. Misuse of funds, in particular activity fund, PPEL, and 67.5 cent schoolhouse. Remember that schools operate under Dillon's Rule. The Code lists what PPEL and 67.5 cent schoolhouse moneys can be used to pay. If something the district wants to do is not in the list, then it cannot be done with those moneys. Generally, if it is not in any Code list, then it becomes a General Operating Fund expenditure, providing it is appropriate from public funds. Activity Fund has always been troublesome because it has been used inappropriately as a clearing account for various other funds. Training on this fund will be provided at the Budget/CAR workshops.
3. Payroll handling. There are a variety of comments regarding payroll. One significant problem is the determination of taxable and nontaxable income. If employees are reimbursed for business expenses

through a non-accountable plan, then all reimbursements are taxable income. Many wellness programs are set up in such a way that they are generating taxable income. If a person who is more than a half-time employee of the district, performs any other services, those services must be included in payroll and may not be paid as if contracted services. Most districts are identifying and reporting employees who serve as referees but are missing other services such as painting, mowing, and computer repair.

CARS

199 of 397 districts filed electronically (50%)! Fantastic!

According to Mary, the CARs are greatly improved over last year even though the edits are more precise. Edit letters are being sent throughout December. At the end of each edit letter is the total edit count for that CAR. Please send the corrections or explanation as soon as possible. Also return the edit letter with the name and phone number of the individual making the changes

ANNUAL SALARY PUBLICATION

Iowa Code section 279.35 requires that the salaries of all regularly employed individuals in the district must be published annually. An Attorney General's Opinion indicates that salaries can be published at any time as long as it is done once annually. Most districts choose either the fiscal year end or the calendar year end. If your district publishes on the calendar year basis, do not use W-2 figures which have been adjusted. The salaries to be published are the total salaries before salary reductions or deductions. Be sure to include all payments for services performed by all employees regardless of what fund was used to account for the payments

TAX LAW UPDATES & REMINDERS

Moving Expense Reimbursement

Reimbursement of deductible moving expenses incurred after December 31, 1993, is reported in box 13 of the W-2 with the Code "P." This is the non-taxable amount and is not included in income.

Deductible moving expenses are limited to the following: transportation and storage of household goods and personal effects, and travel and lodging (not meals) for moving from the old to the new home.

All other payments must be included in the employee's income and are no longer deductible. These payments are reported in box 1 of the W-2 and are to have all appropriate payroll taxes withheld.

As the employer, be sure to complete Form 4782 on the moving expense payments and give to the employee.

Club Dues

Proposed regulations have been released which define which club's dues will no longer be deductible as passed in the Revenue Reconciliation Act of 1993 The proposed regs state that the dues disallowance applies to business luncheon clubs and airline and hotel clubs but generally not to professional organizations or civic or public service organizations. It further states that organizations similar to professional organizations such as chambers of commerce are generally excepted from the dues disallowance unless a principal purpose of the organization is to conduct entertainment for members and guests or to provide access to entertainment facilities. See volume 1994-1 of this newsletter for more information

Meal Reimbursement

When meals are reimbursed which were not related to overnight travel, those reimbursements are taxable income to the employee and are reported on the W-2 even under an accountable plan.

Earned Income Credit

Eligibility for earned income credit was expanded for 1994 To receive advanced payments the employee must file a Form W-5. This form can be filed with only one employer and is valid for only one calendar year. To continue receiving advanced payments, the employee must file a new Form W-5 each calendar year

Circular E

Circular E is in a two-year revision to streamline the publication and make it user friendly. The information removed from Circular E has been moved to other publications such as Publication 937, Employment Taxes, and a new publication not yet available

Form 945

Form 945 is new for 1994. It is an annual report for reporting withholding on other than wages: withholding on pensions, annuities and IRAs, withholding on military retirement, on gambling winnings, and backup withholding. These items are no longer included on Form 941.

Form 1099-MISC

a. Required for each person to whom is paid at least $600 in rents, services, prizes and awards, other income payments and medical and health care payments,

b Required for any federal income tax withheld under the backup withholding rules, c Only payments made in the course of a trade or business are reported This includes payments made by federal, state or local government agencies and nonprofit organizations

IRS Announcement 94-112

The IRS has completed guidelines for examination of colleges and universities. Some of the items specifically discussed are 403(b) annuities, private activity bonds, cafeteria plans and employment tax issues. There is not yet an audit guide for IRS examinations of K-12 districts.

GAAP UPDATE

Eighteen months and counting. That's how long is left before the requirement to comply with GAAP begins.

In 1989, the Iowa legislature passed a requirement that Iowa school districts comply with GAAP beginning on July 1, 1996. The state itself, cities and counties had gone to GAAP earlier

Although the law states that districts shall **comply** with GAAP, the DE has interpreted that more loosely. It has been interpreted as meaning that all reports, interim and year end, have to comply with GAAP and all daily transactions have to be handled in such a way that they would be appropriate when the records were adjusted from cash basis to GAAP basis; but that districts could otherwise operate day to day on a cash basis and only adjust to GAAP for official reports.

In order for the official reports and the CAR to be accurate, this adjustment from cash to GAAP would be necessary at the chart of accounts level, not aggregate level as is used in audits.

Reporting and budgeting are two different issues from two different Code chapters. The law affects district audits, CARs, and other reporting, but does not affect Chapter 24 of the Code which is budgeting. Districts are required to report on the GAAP basis beginning with Fiscal Year 1997 which begins on July 1, 1996 Districts can not choose any other method of **reporting**.

For **budgeting**, however, the Department of Management does not require that budgets be prepared on the GAAP basis. Districts may choose whether to budget on the cash basis or the GAAP basis Once a district chooses the GAAP basis, it cannot change its basis of budgeting. If a district chooses to continue budgeting on the cash basis, the election is made on the CAR where the district will report cash-basis information in one section for this purpose. The rest of the CAR will be completed on the GAAP basis.

FINANCIAL HEALTH STUDY

Mike Hamilton has asked several times about releasing the results of the financial health study conducted on Iowa schools. The study used stepwise multiple regression analysis, basic statistics and correlations, and it received the Clifford Bell Research Award Here is a synopsis of the study.

All Iowa districts were included in the study which used 1990 data from information submitted by districts on reports to the Department of Management or the Department of Education. As part of the study, every state department of education and every U S territory was contacted for copies of published or unpublished studies conducted on their districts, and for copies of their laws, regulations and definitions related to financial health and management. We obtained information on districts taken over by their states and districts which declared bankruptcy. I met the comptroller for the school district in Richmond, California and discussed the events that led to its bankruptcy and what steps had been taken to return it to a solvent position We obtained and read every dissertation listed on this subject (approximately 10). From all that information and information from experts in the for-profit world, from municipal bankruptcies, and from bonding raters, a list of raw data and ratios to be examined was developed. Generally, the Operating Fund was used for data; when other Funds were used, it is so noted.

In effect, the study was conducted four times, using four different measures or definitions of financial health. The first measure used was the level of the unreserved fund balance per certified enrollment The second measure used unspent budget authority to total budget authority. The third measure added together the unreserved fund balance and the unspent budget authority and divided that sum by the certified enrollment. The fourth measure treated unspent balance as if it were a receivable or payable, as appropriate, and recalculated what the unreserved fund balance would be. It added the excess (deficit) of unspent authority over (under) cash balance to the unreserved fund balance and then divided that sum by the certified enrollment

When the **definition of fiscal health was the level of unreserved fund balance per certified enrollment,** the following variables were selected by the procedure in this order:

1. Ratio of total resources to total expenditures
2. Ratio of total liabilities to total assets.
3. Interest revenues less interest expenditures per certified enrollment.
4. Ratio of total object "other expenses" to total expenditures
5. Ratio of cash and investments to total assets.
6. Total revenues per certified enrollment
7. Total expenditures per certified enrollment.
8. Ratio of net income to total revenues.

9. Ratio of Chapter 1 and special education expenditures to total expenditures.
10. Mils of assessed valuation per certified enrollment.

When the **definition of fiscal health was the level of unspent budget authority to total budget authority,** the following variables were selected by the procedure in this order:
1. Ratio of total resources to total expenditures.
2. Total revenues into the General Statutory Fund, without Operating Fund, per certified enrollment.
3. Ratio of revenues from federal sources to total revenues
4. Ratio of salary and fringe benefit objects to total expenditures
5. Total Schoolhouse Statutory Fund revenues, without the Capital Projects Fund or Debt Service Fund, per certified enrollment.
6. Ratio of net income, without regard to interest revenues or expenditures, to total revenues.
7. Ratio of interest revenues less interest expenditures to total budget authority
8. Ratio of total liabilities to total assets

When the **definition of fiscal health added together the unreserved fund balance and the unspent budget authority**, the following variables were selected by the procedure in this order:
1. Ratio of total resources to total expenditures.
2. Interest revenues less interest expenditures per certified enrollment
3. Ratio of the object "other expenses" to total expenditures
4. Ratio of total liabilities to total assets.
5. Ratio of interest revenues less interest expenditures to total budget authority.
6. Total General Statutory Fund revenues, without Operating Fund, per certified enrollment
7. Ratio of salary and fringe benefit object expenditures to total expenditures.
8. Ratio of receivables to total assets.
9. Total Schoolhouse Statutory Fund revenues, without Capital Project Fund or Debt Service Fund, per certified enrollment.
10. Short term debt outstanding at fiscal year end per certified enrollment

When the **definition of fiscal health was the unreserved fund balance adjusted by the excess (deficit) of the unspent authority over (under) cash balance**, the following variables were selected by the procedure in this order:
1. Ratio of total liabilities to total assets
2. Ratio of total resources to total expenditures.
3. Ratio of cash and investments to total assets.
4. Ratio of receivables to total assets.
5. Interest revenues less interest expenditures per certified enrollment.
6. Ratio of salary and fringe benefit objects to total expenditures.
7. Short term debt outstanding at fiscal year end per certified enrollment.
8. Total General Statutory Fund revenues, without Operating Fund, per certified enrollment.
9. Total General Statutory Fund revenues per certified enrollment.

Variables related to revenue sources appeared to show that utilizing alternative funds such as the Management Fund, the Playground Fund, and the PPEL fund to take pressure off the Operating Fund is one aspect of remaining within the authorized budget limits. Several of these variables might measure funding adequacy.

Variables related to expenditures included the relationship of total resources to total expenditures. This was significant and selected in all models, indicating that living beyond (or within) one's means is the single most important aspect related to fiscal health. The second most significant expenditure variable was the cost of salaries and benefits to total expenditures which was retained in the three models which were based on cash flow and was selected but not retained in the model which was based on unspent balance alone. Special education costs affected immediate cash flow but did not affect overall budget authority. Selected twice was the object "other expenses." In 1990, this object included insurance and interest. Insurance was a separate variable which was not selected in any model, which would indicate that it was the interest expenses which caused this variable to be selected.

Variables associated with assets measured the portion of assets which were liquid (cash and investments) and the portion which were receivables, and the portion which were debtor financed. The debtor financed variable was selected in all models

Several **variables were associated with debt**. No model selected new short term debt committed nor selected changes in short term debt outstanding, but all models selected one form of measuring net interest. The models appeared to distinguish between borrowing for cash flow (good cash management) and borrowing for continued existence or living beyond one's means (poor cash management).

The models using unspent balance in the definition did not select variables based on unreserved fund balance. Likewise, models using unreserved fund balance in the definition did not select variables based on unspent balance. This may indicate that the two balances are more dissimilar than is commonly presumed in Iowa financial circles.

Only once was a variable associated with assessed valuation selected. None of the variables associated with staffing ratios, trends, density/sparsity, local wealth, economy of size, or enrollment size was selected

Variables selected in more than one model included total resources to total expenditures, the portion of assets which are debtor financed, the portion of assets which are liquid, the portion of assets which are receivables, short term debt outstanding at fiscal year end, salaries and fringe benefits as a percent of total expenditures, net interest activity, and the use of alternative revenues. Each of these is a reflection of local management decisions. The study concluded that this may suggest that the key to financial stability is the presence of a financial manager who recognizes, monitors, and communicates the district's financial condition, who negotiates effectively, and who manages cash and debt appropriately. This parallels the findings of half the major studies on school district fiscal health reviewed during this study.

For all the wealth of information and computer resources available for this study, the results were disappointing. Nothing was identified that a good auditor couldn't have identified during the annual audit. Other than the one instance where assessed valuation was selected, the variables which were related to financial health were those over which LEA management has considerable control.

The study **recommended that local decisionmakers consider the following** in their management policies:

1. Seek alternative sources of funding such as grants and levies to reduce the stress on the Operating Fund,
2. Limit expenditures to resources.
3. Maintain a positive unreserved fund balance.
4. Maintain a positive unspent authority balance.
5. Limit debt for current expenditures to borrowing against current, but not future, revenues.

The study also confirmed the data distortions caused by the miscoding of revenues and expenditures by districts and by the use of the cash basis of accounting.

The results of the study seem to support the moves the legislature has made to increase the skill level of school financial managers such as requiring compliance with GAAP beginning July 1, 1996, and the tougher requirements for handling of investments in Chapter 12B.

Although the findings based on 1990 data seemed to point to financial management as a significant player in fiscal health or lack of it, there is a flip side to that. Since 1990, school district health has steadily improved. Yet resources have not increased even at the rate of inflation or salary settlements and costs have not declined. This improvement seems to also be the result of school financial management. Other indicators also seem to support that skill is increasing steadily: the audit comments show marked improvement in financial operations each year, the CARs are much better, more districts computerize operations and records each year allowing for more analysis, the number of managers back in college night courses, and the number of managers attending the IASBO Academy. Five years ago, many phone calls were questions which were fairly easy to answer on the spot. Now many questions require more time, research and statistical analysis to answer. **District management has every right to be proud of its achievement.**

Have a nice holiday! See you at the workshops.

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